



**STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS**

DRAFT

Date Introduced:	02/27/09	Bill No:	<u>AB 1265</u>
Tax:	Sales and Use	Author:	Ma
Related Bills:	SB 809 (Veteran Affairs Committee)		

BILL SUMMARY

This bill would specify that certain United States veterans would be regarded as consumers, rather than retailers, of tangible personal property they sell under specified conditions.

ANALYSIS

CURRENT LAW

Under California's Sales and Use Tax Law (Part 1, Division 2 of the Revenue and Taxation Code, commencing with Section 6001), except where specifically exempted by statute, sales tax is imposed on all retailers for the privilege of selling tangible personal property at retail in this state. The law does not contain a general exemption from sales or use tax for sales of tangible personal property by veterans.

Under the law, every retailer or any other person engaged in the business of selling tangible personal property of a kind the retail sale of which is taxable in this state is required to obtain a seller's permit and report the tax on his or her sales on a return prescribed by the Board. However, California's Sales and Use Tax Law places a variety of retailers making taxable sales of tangible personal property under a "consumer" reporting status. Under a "consumer" reporting status, a qualifying retailer making otherwise taxable sales is not required to obtain a seller's permit or report tax on those sales. Rather, the qualifying retailer is only required to pay tax on his or her cost of the taxable components of the products he or she sells.

The "consumer" reporting status is primarily intended to minimize reporting burdens placed on smaller businesses and entities, while minimizing the associated revenue loss that can accompany a complete exemption from the tax. The law has extended this consumer reporting status to certain sales by such entities as nonprofit youth groups, PTAs, nonprofit veterans' organizations, various charitable organizations, schools and school districts, optometrists, veterinarians, podiatrists, licensed hearing aid dispensers, and others with respect to certain products they sell.

PROPOSED LAW

This bill would add Section 6018.3 to the Sales and Use Tax Law to specify that a "qualified itinerant vendor" is a consumer of, and shall not be considered a retailer of, tangible personal property owned by the qualified itinerant vendor, except alcoholic beverages.

The bill would specify that a person is a "qualified itinerant vendor" when all of the following apply:

- 1) The person was a member of the United States Armed Forces, who received an honorable discharge or a release from active duty under honorable conditions from service,
- 2) The person is unable to obtain a livelihood by manual labor due to a service-connected disability.
- 3) For the purposes of selling tangible personal property, the person is a sole proprietor with no employees, and
- 4) The person has no permanent place of business in this state.

The bill would define “permanent place of business” as any building or other permanently affixed structure, including a residence that is used in whole or in part for the purpose of making sales of, or taking orders and arranging for shipment of, tangible personal property, and would exclude from that term, any building or other permanently affixed structure, including a residence, used for any of the following:

- 1) The storage of tangible personal property.
- 2) The cleaning or the storage of equipment or other property used in connection with the manufacture or sale of tangible personal property.

The bill would specify that its provisions do not apply to either of the following:

- 1) A person engaged in the business of serving meals, food, or drinks to a customer at a location owned, rented, or otherwise supplied by the customer, or
- 2) A person operating a vending machine.

The bill would become operative on the first day of the first calendar quarter commencing more than 90 days from the bill’s effective date.

BACKGROUND

For the past 11 years or so, several veterans have argued that state law which exempts honorably discharged veterans from locally-imposed license taxes and fees also exempts itinerant veterans from any tax imposed by the state. More specifically, it has been argued that Business and Professions Code Section 16102 exempts honorably discharged veterans from application of the sales and use tax on sales of food products and carbonated beverages from a mobile food cart. This section reads in its entirety as follows:

“Every soldier, sailor or marine of the United States who has received an honorable discharge or a release from active duty under honorable conditions from such service may hawk, peddle and vend any goods, wares or merchandise owned by him, except spirituous, malt, vinous or other intoxicating liquor, without payment of any license, tax or fee whatsoever, whether municipal, county or State, and the board of supervisors shall issue to such soldier, sailor or marine, without cost, a license therefore.”

This provision was enacted in 1893 pursuant to AB 74, and was described in the chaptered bill as “An act to establish a uniform system of county and township government.” In its present form (which has remained unchanged since 1941) Section 16102 falls within Chapter 2 of Part 1 of Division 7 of the Business and Professions Code, entitled *Licensing by Counties*.

In 1999, the Board held that this provision does not apply to sales or use taxes imposed pursuant to California's Sales and Use Tax Law. The Board's decision was subsequently challenged unsuccessfully in Los Angeles Superior Court (No. BC 210257). The Board's decision is also consistent with that of the Office of Legislative Counsel in its two opinions specific to this issue rendered in 1998 and 2006, concluding that the exemption provided in this section only applies to county license tax and license fees, and does not apply to sales and use taxes.

COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the author to specifically address the application of the Sales and Use Tax Law to itinerant disabled veterans who themselves make sales of goods they own, such as handcrafted items, paintings, memorabilia, and blankets. Specifically, this bill would deem these veterans to be consumers of the products they sell, and provide for the payment of taxes at the point these veterans purchase the component parts of the items they sell, to the extent the tax applies. The purpose of this bill is to recognize and honor service-disabled veteran survivors that are seeking to make a living by itinerant sales of goods. This bill would apply to veterans of past conflicts as well as veterans returning from foreign conflicts in which the United States is currently engaged.
2. **What would a qualifying veteran's tax obligations be?** Under this bill, a qualifying itinerant disabled veteran making taxable sales of goods, wares or merchandise owned by him or her would not be required to report sales tax on his or her sales of these items. Instead, those veterans would only be required to pay tax on their cost of any taxable purchases of the items or the component parts of the items he or she sells. For example, if a veteran were selling his or her own paintings, the veteran would pay tax on his or her purchase of the paint, brushes, and canvas used to make the painting. The sale of the painting, itself, would thereafter be exempt from tax. Under this measure, if the qualifying veteran makes no sales of alcoholic beverages, the veteran would not be required to obtain a seller's permit, file sales tax returns, or remit sales tax on his or her sales of the goods he or she sells. This essentially eliminates the sales tax compliance costs and associated recordkeeping that can be unduly burdensome for disabled veterans.
3. **Qualifying veterans would need to provide evidence of disability to qualify.** Up until January 1, 2009, Business and Professions Code authorized cities to issue business licenses to honorably discharged or honorably relieved United States veterans without payment of any business license tax or fee for their sales of goods they own, provided, among other things, the veteran was physically unable to obtain a livelihood through manual labor (however, the law did not require that the veteran have a service-connected disability). Although this qualification is no longer necessary through enactment of AB 1952 (Stats. 2008, Ch.435), we contacted several cities to determine how they administered Section 16001.5 prior to January 1, 2009. The cities that we contacted indicated that they required the veteran to provide confirmation from a physician that he or she had such a physical impairment. If this bill becomes law, we expect that we would require a similar physician confirmation of the veteran's disability. Also, since the bill would require that the disability be service-related, we would require that a qualifying veteran also provide written confirmation of that disability from the Department of Veteran Affairs.

4. **Bill would not be problematic to administer.** The bill would apply to a small group of itinerant disabled veteran vendors. If this bill becomes law, the Board would no longer require these individuals to hold a seller's permit.
5. **Related legislation.** SB 809 (Veteran Affairs Committee) also contains provisions on this issue. However, unlike this bill, SB 809 would provide a complete exemption for similar items sold by itinerant disabled veterans in a similar manner.

COST ESTIMATE

We estimate that the administrative costs associated with this measure attributable to identifying and notifying affected veterans, closing permits, and amending the Board's affected regulations would be absorbable.

REVENUE ESTIMATE

BACKGROUND, METHODOLOGY, AND ASSUMPTIONS

Board staff estimates that taxable sales, excluding alcoholic beverages, that were made by itinerant vendors were about \$1,873 million in 2005. We estimate that about 9.3 percent of these sales were made by veterans, for a total of about \$174 million in taxable sales. Of these, we estimate that about 7 percent of the sales were made by disabled veterans - about \$12.2 million in taxable sales.

Using national sole proprietor sales data from the U.S. Census Bureau 2002 U.S. Economic Census, we distributed this \$12.2 million in taxable sales among five North American Industry Classification System (NAICS) industries that we concluded would constitute itinerant vendor sales. These industries are: caterers, mobile food services, vending machine operators, other fuel dealers, and other direct selling establishments. Two of these five industries were determined to be industries where the taxpayers would meet the requirements of this bill: (1) mobile food services and (2) other direct selling establishments. Mobile food services accounted for about 6 percent of sales of these five industries. Other direct selling establishments were responsible for about 60 percent of the sales of these five industries. Of the \$12.2 million in sales of the five itinerant vendor industries, mobile food services and other direct selling establishments combined accounted for \$8.0 million in taxable sales.

We also used these Census Bureau data and a publication from the U.S. Bureau of Economic Analysis to estimate purchases by these businesses for which the retail markup margins would no longer be subject to tax under this measure. The taxable portion that would be exempted by this bill for these two industries were estimated to be about \$4.9 million of the \$8.0 million in taxable sales under current law. About \$4.2 million (86 percent) of the \$4.9 million are from sales of other direct selling establishments. The remaining \$0.7 million (14 percent) are from sales of mobile food services.

We also adjusted sales made by other direct selling establishments to exclude direct selling of furniture, home furnishings, electronics and appliances. These products were determined to be too bulky to sell from a temporary location without inventories. This adjustment reduced sales of other direct selling establishments by about 25 percent,

from \$4.2 million to \$3.2 million. At this point, the exempt portion totals \$3.9 million, including the \$0.7 million of mobile food services sales.

We estimated the proportion of sales made by sole proprietors without employees, also using data from the 2002 U.S. Economic Census. These data indicate that about 38 percent of sales made by mobile food services were made by sole proprietors without employees. Assuming this percentage, of the \$3.9 million in exempt sales, we estimate that about \$1.5 million are from sole proprietors without employees.

The U.S. Bureau of Labor Statistics has U.S. labor force participation rates for veterans with less than and more than a 30 percent disability rating. We assume these participation rates also hold for California sole proprietors. We also obtained data on numbers of California disabled veterans by age and disability rating group for all disabled veterans and those veterans with general medical and surgical disabilities from the U.S. Veterans Administration. For revenue estimation purposes, we assume that a person who is unable to obtain a livelihood by manual labor due to a service-related disability has a general medical and surgical disability rating of 30 percent or more. About 83 percent of the \$1.5 million in exempt sales were made by disabled veterans have general medical-surgical disabilities. Using the labor force data, about 23 percent of these disabled veterans have disability ratings of 30 percent or more and are in the labor force. Under both of these criteria, we estimate that taxable sales for veterans qualified under this bill amount to about \$277,000.

REVENUE SUMMARY

The annual revenue loss from defining qualified veterans as consumers of taxable items is about \$25,000. The following table shows how these revenues are distributed among the various funds:

	Rates	Dollars
State	6.25%	\$17,337
General Fund	6.00%	\$16,644
Fiscal Recovery Fund	0.25%	\$693
Local	2.00%	\$5,548
Transit	0.71%	\$1,970
Total State and Local	8.96%	\$24,855

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